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CITATIONS

Cases:

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In the Supreme Court of the United States

OCTOBER TERM, 1962

Nos. 108, 109, 110, 125

INTERSTATE COMMERCE COMMISSION, ET AL., APPELLANTS

v.

NEW YORK, NEW HAVEN AND HARTFORD RAILROAD COMPANY, ET AL.

ON APPEALS FROM THE UNITED STATES DISTRICT COURT FOR THE DISTRICT OF CONNECTICUT

BRIEF FOR THE UNITED STATES

OPINIONS BELOW

The opinion of the district court (R. 241–262) is reported at 199 F. Supp. 635. The opinion of the Commission (R. 4–69) is reported at 313 I.C.C. 23.

JURISDICTION

The judgment of the three-judge district court (R. 263–264) was entered on January 8, 1962, and notices of appeal were filed by the United States (R. 268–270), the Interstate Commerce Commission (R. 264–266), Sea-Land Service, Inc. (R. 266–268), and Seatrain Lines, Inc. (R. 271–272) on March 9, 1962. This Court's jurisdiction on direct appeal is conferred by 28 U.S.C. 1253 and 2101(b), and is sustained by *United States* v. *Central Vermont Ry., Inc.*, 366 U.S.

272, and *Interstate Commerce Commission* v. *J–T Transport Co., Inc.*, 368 U.S. 81.

STATUTES INVOLVED

The National Transportation Policy, 49 U.S.C. preceding Section 1, and Sections 15(7) and 15a of the Interstate Commerce Act, 49 U.S.C. 15(7), and 15a, are set forth in the Appendix, *infra*, pp. 51–54.

QUESTIONS PRESENTED[1]

Appellee railroads proposed substantially reduced rates for trailer-on-flatcar ("TOFC") service between certain points also served by coastal water carriers. The water carriers' fully distributed costs of moving the traffic involved were, in almost all instances, below the fully distributed costs of the railroads' TOFC service. The reduced rates, which exceeded the railroads' out-of-pocket costs in all cases and in many instances exceeded their fully distributed costs, were at the level of the water carriers' rates for the same traffic, but were substantially below the level maintained by the railroads for similar traffic between points not served by the water carriers. The Interstate Commerce Commission cancelled the reductions on the grounds that the water carriers could not compete with railroads at equal rates; that the reductions were the initial step in a general rate-cutting program which threatened the water carriers' continued exist-

[1] Although the precise formulation of the questions here differs from that in our Notice of Appeal and Jurisdictional Statement, we believe that the questions as presently stated reflect "the substance of the questions already presented" within the meaning of Rule 40(1)(d)(2) of the Revised Rules of this Court.

ence; and that the water carriers were essential to national defense and an integral part of the national transportation system. The district court reversed.

The questions presented are:

1. Whether, in the light of the National Transportation Policy and Section 15a(3) of the Interstate Commerce Act, the Commission was precluded from cancelling the reduced rail rates on economic grounds, without a finding that they interfered with the right of the water carriers to realize an inherent advantage of cost or service which they possessed.

2. Whether, if no such inherent advantage is infringed by the TOFC rates at issue, the Commission might nonetheless cancel them on the ground that they threaten the survival of a mode of transportation whose continued existence is required to meet the needs of the national defense, the postal service, or the commerce of the United States.

STATEMENT

This case involves the validity of an order of the Interstate Commerce Commission directing the cancellation of substantial reductions proposed by several railroads on some 66 commodity rates for trailer-on-flatcar (TOFC) service between various points in the East, on the one hand, and Dallas and Ft. Worth, Texas, on the other. The proposed rates were limited to points served by the only deep-water common carriers now engaged in the Atlantic-Gulf coastwise trade, Sea-Land Service, Inc. (formerly Pan-Atlantic Steamship Corporation) and Seatrain Lines, Inc.

1. THE COMPETING CARRIERS

Sea-Land provides an Atlantic-Gulf coastwise service by motor-water-motor. Freight is moved by certificated motor carriers (or by use of Sea-Land's own motor equipment) in highway trailers over the road to the port of origin, where the trailers are lifted onto Sea-Land ships for movement via water to the destination ports. At the destination ports, the process is reversed. This service was instituted by Sea-Land in 1957 when substantial increases in its operating costs as a break-bulk [2] water carrier led it to suspend its Atlantic-Gulf break-bulk service and to convert four vessels into trailerships, each capable of holding 226 demountable truck trailers. Conversion to the more efficient trailership service has reduced Sea-Land's operating costs and has brought about a reduction in both cargo-handling time and in-port vessel time (R. 7–10, 79–84, 168–176, 243).

Seatrain provides Atlantic-Gulf coastwise service by rail-water-rail. Freight is transported to its dock at Edgewater, New Jersey, in railroad cars. The cars and their contents are then lifted onto Seatrain's vessels for carriage by water to Atlantic and Gulf ports. The cars then move by rail to the consignee. This service offers the shipper transportation in a single rail car from consignor to consignee (R. 243).

The railroad TOFC service involved here is a motor-rail-motor operation in which a motor carrier trailer loaded by the shipper is hauled by road to a

[2] Break-bulk service involves the physical unloading of freight from rail-car or truck into ships at the port of origin and the reverse operation at destination.

railhead, where it is loaded onto a flatcar, and demounted at destination for delivery by motor carrier to the consignee. Although this type of service has been furnished sporadically since 1926, it has grown in recent years, and the TOFC service between the points covered by this proceeding was inaugurated in the summer of 1956 (R. 244).

Traditionally, water rates, including water-rail and water-motor rates, have been lower than the corresponding all-rail rates. Water service has also been slower, less frequent, and more perilous (R. 10-11, 87, 179). When Sea-Land inaugurated its new trailership service in 1957, it published rates which were, in general, 5 to 7½ per cent lower than the corresponding all-rail boxcar rates, a narrower differential than that which had theretofore existed (R. 11–12, 88, 180–181, 243).

By schedules filed to become effective on November 14, 1957, and later, the railroads proposed to establish reduced TOFC rates for numerous commodities between points in the East and in Texas, which were approximately at the level of Sea-Land and Seatrain rates on the same traffic. Upon the protests of the Secretary of Agriculture, Sea-Land, Seatrain, and other interested parties, the rates were suspended and

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[2] Since the establishment of these rates would leave higher rates in effect to and from intermediate points involving shorter hauls in violation of the long-and-short-haul provisions of Section 4(1) of the Act, 49 U.S.C. 4(1), the railroads also applied to the Commission for the relief from those provisions which Section 4(1) permits the Commission to authorize "in special cases." See *A. L. Mechling Barge Lines, Inc.* v. *United States*, 368 U.S. 324.

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placed under investigation. On December 19, 1960, the Commission issued its report and accompanying order.

2. THE COMMISSION'S DECISION

The Commission found that the proposed TOFC rates equaled or exceeded out-of-pocket costs for all listed movements by railroad-leased TTX[*] cars and for all but six movements by railroad-owned cars, and equaled or exceeded fully distributed costs for 43 of 66 movements by TTX cars and for 14 of 66 movements by railroad-owned cars (R. 22). The Commission concluded, therefore, that with the exception of the six rates returning less than out-of-pocket costs—rates which were withdrawn by the railroads and are not at issue here—the proposed rates were compensatory (R. 22, 34). Similarly, the corresponding Sea-Land and Seatrain rates—whose legality is not challenged in this proceeding—were, with one exception, found to be compensatory (R. 21-22, 23-25).

The Commission then turned to the question "whether these rates constitute destructive competition" (R. 34). With respect to the relative costs of the competing modes of transportation, the Commission found that Sea-Land's costs of moving the traffic, both out-of-pocket and fully distributed, are uniformly below the railroads' costs for similar

[*] TTX cars are flatcars leased by the railroads which hold two trailers; railroad-owned cars have a capacity of one trailer per car (R. 21). No finding could be made as to the relative percentages of traffic which would move under the proposed rates in either type of car (R. 22).

TOFC movements using railroad-owned flatcars, and are below the TOFC costs using TTX cars for all but two of the 66 movements (R. 21, 36). However, the Commission indicated that it was not resting its decision on relative costs. Because of certain variables affecting costs and the absence of rail cost data relating to rates for all-rail boxcar service, the Commission said that it was unable to determine whether rail boxcar, TOFC, Sea-Land, or Seatrain was the lowest cost mode of transportation. The Commission further said: "We must recognize, also, that cost is only one of the elements which may appropriately be considered in passing upon the lawfulness of rates. In the exceptional circumstances here presented, other considerations, herein discussed, appear to us determinative of the issues" (R. 37).

The Commission found that the perils of ocean transport, infrequency of sailings, and transit time longer than that in rail TOFC service are factors in both Sea-Land and Seatrain Service (R. 11, 13, 27-28); that, by reason of these factors, Seatrain offers a lower-quality service than TOFC (R. 25–27); that there is no indication that Sea-Land has moved any traffic at rates as high as competing rail boxcar or TOFC rates (R. 22, 34); that most shippers prefer railroad service to Sea-Land and Seatrain, which must accordingly maintain rates lower than those of the rail carriers (*ibid.*). It also found that all of the water carriers' service is subject to rail competition while, for the railroads, the competitive traffic is only a small portion of their total traffic. Therefore, the Commission held, if the lower rates which the water

carriers are competitively required to maintain are reduced to a point which fails to yield operating costs plus a reasonable return on investment, their operations will become unprofitable and their continuance will be jeopardized (R. 35). Finally, the Commission found that the "reduced rates of the railroads here under consideration are an initial step in an overall program of rate reductions that can fairly be said to threaten the continued operation, and thus the continued existence, of the coastwise water-carrier industry generally" (R. 38). The Commission made no finding, however, as to whether reductions in the water carriers' rates to reinstate the differential wiped out by the railroad rate reductions would make the water rates unprofitable. Nor did it find whether the water carriers' rates on the particular traffic involved here should yield more than cost plus a reasonable return on investment in order to compensate for the carriage of other and less remunerative traffic.

Turning to the statutory criteria, the Commission cited Section 15a(3), as prohibiting the maintenance of a carrier's rates at a particular level in order to protect the traffic of another mode of transportation. It noted, however, that this prohibition is qualified by the words "giving due consideration to the objectives of the national transportation policy declared in this Act" (R. 37).

The Commission observed (R. 38–41) that the importance of coastwise shipping for national defense purposes has been repeatedly emphasized by various governmental agencies (citing a published statement of the Maritime Administration and a Senate Com-

mittee report) and that it is an integral element of the national transportation system (citing ICC decisions and shipper evidence that at lower rates the water carriers will attract traffic). The Commission reasoned, moreover, that Sections 305(c) and 307(d) of the Act, 49 U.S.C. 905(c), 907(d) are indicative of a Congressional intent to accord an essential and efficiently operated water carrier an "advantage in the form of lower rates", where this was necessary to enable it "to participate in the economical movement of traffic" (R. 40).

The Commission concluded (R. 41):

> In the circumstances presented here, we are of the opinion that the objectives of the national transportation policy require the establishment and maintenance of a differential relationship between the rates under investigation on Sea-land and Seatrain service, on the one hand, and the rates of the rail carriers, on the other, which will allow these water carriers operating in the coastwise trade to maintain rates that will enable them to continue efficient and economical coastwise service.

While it considered the 10 per cent differential sought by Sea-Land to be excessive, the Commission stated that, in its judgment, the TOFC rates at issue should be held at 6 per cent above Sea-Land's rates so long as the latter are not increased above their present levels (R. 41–42). Accordingly, the Commission found that the proposed TOFC rate reductions were not shown to be just and reasonable and directed their cancellation without prejudice to the filing of new schedules in conformity with the Commission's conclusions (R. 42).

Three Commissioners dissented and urged that the record did not support a rate differential to protect the water carriers involved (R. 43–45). One Commissioner concurred in part, stating that he would approve all compensatory rates without imposing a differential (R. 43).

3. THE DISTRICT COURT'S DECISION

On February 1, 1961, the railroads filed their complaint in the district court seeking to set aside the Commission's order to the extent that it required cancellation of the proposed TOFC rates. Sea-Land and Seatrain intervened to defend the order. On November 15, 1961, the three-judge court rendered its opinion, holding that the order requiring cancellation of the TOFC rates should be set aside and that the Commission should be enjoined from cancelling TOFC rates which return the fully distributed costs of carriage (R. 258).

The court held that to require a differential between rail and water rates merely for the protection of the water carriers would be a violation of Section 15a(3), and that the National Transportation Policy did not warrant a different conclusion on this record (R. 246–247). It stated that a carrier's rates cannot be held to be "a destructive competitive practice", even though they threaten the existence of a competitor, unless they are (a) so low as to be hurtful to the proponent as well as its competitor; or (b) so low as to deprive the competitor of the "inherent advantage" of being the long-run lower-cost mode of transportation (R. 251–252). Although the Commission opinion did not so indicate, the court expressed

the belief that the Commission's action in keeping the railroad rates above fully distributed costs was an attempt to preserve a "value-of-service" ratemaking structure, *i.e.*, that Sea-Land's rates were being maintained above fully distributed costs on high-value goods in order to compensate for its failure to recover such costs on other traffic (R. 252–253). The court held that if the decision were based on such a theory it 'must fall for lack of evidence and necessary findings" that Sea-Land's "overall rate structure" was that of the overall low-cost mode" (R. 255).[5]

Finally, the court held that the national defense clause of the National Transportation Policy was merely a "hoped-for 'end' ", not an "operative policy," and that, in any event, the Commission's finding that the proposed rail rates would be inconsistent with the national defense was not supported by the evidence (R. 256–257).

SUMMARY OF ARGUMENT

1. Section 15a(3) of the Interstate Commerce Act presents an ambivalent mandate. Insofar as it prohibits the Commission from maintaining the rates of one carrier at a particular level in order to protect a competing mode of transportation, it proclaims a

[5] The court further stated that, even with respect to traffic for which water is the low-cost mode of carriage, the Commission may disallow TOFC rates covering the railroads' fully distributed costs only if a water rate in excess of the water carriers' fully distributed costs should be maintained to compensate for their carriage of other traffic (for which water is also the low-cost mode) at less profitable rates, and in no event, said the court, may the Commission reject a TOFC rate for a particular movement on which TOFC is the low-cost mode, which covers the railroads' fully distributed costs (R. 258, 259).

policy of free competition. On the other hand, insofar as it qualifies that prohibition by admonishing the Commission to give due consideration to the objectives of the National Transportation Policy, it looks (at least in some degree) in the direction of protectionism. The problem is one of accommodation.

In cancelling the proposed TOFC rates, the Commission relied upon two of the policy factors embodied in the National Transportation Policy: the prohibition of "destructive competitive practices" and the "needs of the commerce * * * and of the national defense." The Commission apparently reached the conclusion that the proposed reductions would constitute a destructive practice forbidden by the Act (a) without giving weight to the relative costs of the two competing forms of carriage; (b) despite a finding that nearly all of the proposed rates exceeded the out-of-pocket costs, and many the fully distributed costs, of the service; and (c) on the ground that the water carriers needed lower rates than the railroads if they were to overcome the handicap of inferior service and attract a "fair share" of the traffic. We agree with the district court that the Commission's order, to the extent that it relied upon the presence of destructive practices, cannot stand. For if Section 15a(3) means anything, it must mean that the Commission is without power to impose a rate differential which bears no relationship to the comparative costs of the two modes, merely to shield the less economical carrier from the normal incidents of competition.

The legislative history, we think, bears out the district court's conclusion that (apart from considera-

tions of commerce and national defense) the prohibition against umbrella rate-making was intended to be relaxed only when necessary to preserve the inherent advantage of a competing low-cost carrier; and that the "destructive competitive practices" forbidden by the National Transportation Policy are those condemned by their predatory character (*e.g.*, rates below out-of-pocket costs) and those which, though perhaps "compensatory," would erode the inherent advantage of a competitor. Adopted in 1958, the amendment represented a compromise between a bill advanced by the railroads which would have precluded the Commission absolutely from considering the effect of a proposed rate upon a competing mode of transportation, and recommendations of the motor and water carriers, as well as the Commission itself, urging that no new legislative restrictions at all be imposed upon the exercise of the Commission's minimum rate power. Although the Senate Commerce Committee expressly rejected the extreme proposal of the railroads—known as the "three shall-nots"—it made clear, nonetheless, that the chief objective of the amendment was to encourage competitive rate-making in the transportation industry and to insure that each mode of carriage would be free to assert its inherent advantages of cost or service.

The legislative history indicates further that the primary purpose of the qualifying provision—referring to the National Transportation Policy—was to meet the objection that otherwise the Commission would be disabled from dealing with rates which were predatory or destructive in the sense that they would

undermine the inherent advantages of competing media rather than assert legitimately the advantages of the rate proponent. Particularly influential was the testimony of Chairman Freas of the Commission before the Senate Commerce Committee, in which he repeatedly focused attention upon the railroads' historic practice of cutting selected rates to levels which—though slightly above out-of-pocket costs—were well below fully distributed costs and consequently inhibited lower-cost competitors from charging a rate which at once reflected inherent advantage and yielded fair return. To remove any doubt as to the power of the Commission to condemn such practices, Chairman Freas suggested language which would have qualified the ban on umbrella ratemaking by instructing the Commission to give due consideration "to the inherent cost and service advantages of the respective carriers." Although the Committee, and later Congress as a whole, formulated the qualification in terms of the National Transportation Policy, rather than "inherent advantages," there is little doubt that their main purpose was to meet the problem raised by Chairman Freas. We conclude, therefore, that the district court was correct in holding that, in the absence of a finding that the water carriers were the low-cost mode on the particular movements involved, the Commission was not entitled to disturb the proposed railroad rates.

2. Although the Commission declared itself unable to determine where the inherent advantages lay as to any of the rates in controversy, and held that considerations other than relative costs were dispositive, it did state that Sea-Land's [redacted] were lower than those of

the corresponding TOFC costs for virtually all of the movements involved. However, even if that statement were deemed to constitute a "finding" that Sea-Land was the low-cost mode, it would still not sustain the Commission's cancellation of those TOFC rates (the only rates now in issue) which exceeded the railroad's fully distributed costs. To warrant protective action, it must be shown not only that the competing carrier possesses an inherent cost advantage, but also that this advantage would be impaired by the proponent's rate.

Such impairment occurs, we submit, when the low-cost carrier is unable to fix a rate which (a) covers its fully distributed costs and (b) affords it a rate advantage (as against the high-cost carrier) which is no less than the cost differential (measured in terms of fully distributed costs) between the two modes. A rate which exceeds the fully distributed costs of the high-cost carrier cannot place a competitor in this predicament and therefore, in ordinary circumstances, cannot be deemed "destructive." That the Commission should not ordinarily be permitted to disallow a fully compensatory rate was brought out in the congressional debates on Section 15a(3).

In some instances, perhaps, the low-cost mode might require for particular movements a rate significantly higher than fully distributed cost in order to offset deficits on other freight which will not move at a fully compensatory rate; in such cases it might be appropriate to maintain a cost-justified rate differential at a higher level than would otherwise be warranted. But the Commission made no findings that

there was need to subsidize the movement of other traffic here.

If it should turn out that Sea-Land, because of its inferior service, were unable to attract substantial business at a differential which no more than reflected its inherent cost advantage, the railroads' ability to provide a better overall bargain, cost and service considered together, would be an inherent advantage to which the public is entitled and which the National Transportation Policy admonishes the Commission to protect, whatever may be the consequences to the water carriers.

3. The district court erred, we believe, in holding that national defense requirements could not independently sustain the Commission's order because defense is mentioned in the National Transportation Policy—not as an operative policy factor, but merely as the hoped-for "end" of the operative policy factors previously enumerated. While the primary purpose of Congress in qualifying the basic prohibition in Section 15a(3) was to preserve "inherent advantages," it is significant that Congress chose not to accept language proposed by the Commission, which would have expressed the qualification in terms of the inherent-advantage factor alone, and instead adopted the broader reference to the National Transportation Policy as a whole. In some instances, for example, a carrier which lacks any widely demanded economic advantage and cannot attract enough business to operate at a profit may yet be uniquely equipped to perform a service vital to the military establishment or possess facilities of great potential importance in the event

of a national emergency. In such circumstances, the prohibition against umbrella rate-making might properly be subordinated to the requirements of national defense. To warrant such action, however, it must be demonstrated that the proposed rate genuinely threatens to destroy a competing mode of transportation and, moreover, that the threatened mode is able to fill a vital national defense need which could not be adequately filled by any other available form of carriage. Such evidence must relate to the specific carrier which seeks protection and should set forth with particularity the reasons why the survival of this carrier is important to the national defense. Since we do not believe the evidence and findings of the Commission here met these standards, we agree that its order was properly vacated. At the same time, we urge that the district court's interpretation of this aspect of the National Transportation Policy is unduly restrictive and that the Commission, upon remand, should have greater latitude than the opinion below would permit.

ARGUMENT

Section 15a(3) of the Act (Appendix, *infra*, pp. 53-54), adopted in 1958 after three years of controversy, represented a compromise between the proposals advanced by the railroads, which would have precluded the Commission from even considering the effect of a rate on a competing mode of transportation and the recommendations of the motor and water carriers, as well as the Commission itself, urging that existing law be left unchanged. The chief thrust of the amendment, as the committee reports confirm, was to encourage competitive ratemaking among the different

modes of carriage. H. Rep. 1922, 85th Cong., 2d Sess., p. 15; S. Rep. 1647, 85th Cong., 2d Sess., p. 3. To that end, Section 15a(3) provides that in fixing minimum rates where there is intermodal competition, the Commission "shall consider the facts and circumstances attending the movement of the traffic by the carrier or carriers to which the rate is applicable"; and that "[r]ates of a carrier shall not be held up to a particular level to protect the traffic of any other mode of transportation." However, engrafted upon this mandate was the qualification that the Commission give "due consideration to the objectives of the national transportation policy declared in this Act." That policy (Appendix, *infra*, p. 51) admonishes the Commission to recognize and preserve "the inherent advantage" of each mode, to encourage the establishment of reasonable rates without unjust discriminations or "unfair or destructive competitive practices," and to "foster sound economic conditions * * * among the several carriers"—"all to the end of developing, coordinating, and preserving a national transportation system * * * adequate to meet the needs of the commerce of the United States, of the Postal Service, and of the national defense."

The Commission's decision in this case rested, in part, on the importance of the coastwise water carriers to the national defense and commerce. As a further ground for its action, however, the Commission appears to have concluded that the proposed railroad rate reductions would constitute a "destructive competitive practice" within the meaning of the Na-

tional Transportation Policy.[6] It reached this conclusion (a) without regard to the relative costs of the two competing modes of transportation;[7] and (b) despite a finding that almost all the rail rates in issue covered the out-of-pocket costs, and many of the fully distributed costs, of carriage. The mere fact that the proposed rates would eliminate the differential needed by the water carriers in order to overcome the handicap of inferior service, and thus attract a "fair share" of the traffic, was apparently deemed by the Commission a sufficient basis for cancelling them.

In setting aside the order, the district court held that the prohibition against compulsory rate differentials in Section 15a(3) was intended to be qualified only by the "inherent advantages" and "destructive

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[6] Thus, the Commission, after noting that all of the rates involved here (with a few exceptions) were compensatory, stated that "[t]he next, and the most important, question is whether these rates constitute destructive competition" (R. 34). And, later, the Commission declared that: "The reduced rates of the railroads here under consideration are an initial step in an overall program of rate reductions that can fairly be said to threaten the continued operation, and thus the continued existence, of the coastwise water-carrier industry generally" (R. 38). See, moreover, the court's characterization of the Commission's opinion (R. 249).

[7] The Commission stated that the Sea-Land costs, both out-of-pocket and fully distributed, were below the restated TOFC costs for nearly all movements to which the TOFC rates would apply. However, it appeared to place no reliance upon this statement. For it also noted that "we cannot determine on these records where the inherent advantages may lie as to any of the rates in issue. We must recognize, also, that cost is only one of the elements which may appropriately be considered in passing upon the lawfulness of rates. In the exceptional circumstances here presented, other considerations, herein discussed, appear to us determinative of the issues" (R. 36–37).

competitive practices" factors of the National Transportation Policy (R. 252), and that the Commission's reliance upon national defense considerations was therefore misplaced. Furthermore, it regarded these qualifying factors as interrelated concepts, a destructively competitive rate being defined, in effect, as one which, if compensatory at all (*i.e.*, above out-of-pocket costs), nevertheless fails to cover fully distributed costs and thereby deprives a competing carrier of the "inherent advantage" of being the low-cost mode (R. 251–252). In the court's view, however, a rate which merely reflects a proponent's competitive superiority is not to be disturbed by the Commission even though its effect might be to render obsolete a competing mode of transportation.

Although the United States supported the Commission's order in the district court, we are persuaded that the cause should be remanded to the Commission. At the same time, we do not agree in all respects with the terms of the district court's remand.

Contrary to the decision below, we urge that the overriding requirements of national defense would justify the Commission, upon proper findings and evidence, in extending minimum-rate protection to a carrier which lacked any inherent advantage and which was not the victim of a forbidden competitive practice. Although we believe that the evidence and findings here were not adequate to sustain the cancellation of these rates on national defense grounds, we submit that those grounds should be left open to the Commission upon remand.

In the absence of national defense considerations, however, we agree with the district court that the Act

does not empower the Commission to impose rate differentials between competing modes of transportation merely to shield the less economical carrier from the normal incidents of competition or to assure it a "fair share" of the traffic. The paternalistic regulatory philosophy reflected in the Commission's decision here is fundamentally at odds with the policy of free competition Congress proclaimed in Section 15a(3). That Section, as qualified by the National Transportation Policy, tolerates the imposition of rate differentials only to the extent justified by relative costs and (subject to the qualification noted *infra*, pp. 41–42) at levels no higher than necessary to enable the low-cost carrier to recover its fully distributed costs for the service in question.[8]

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[8] In the court below the United States asserted that the selective character of the rate reductions at issue, which were instituted only on routes where the railroads face water competition, provided a further basis for their cancellation by the Commission as unfair or destructive competitive practices. Upon further consideration, we no longer adhere to that position. The Commerce Act itself provides relief against those rate discriminations which result in secondary-line competitive injury (*i.e.*, to shippers), specifically foreclosing consideration of injury to competitors of the carrier in terms of discrimination (see 49 U.S.C. 2, 3, and comparable provisions under Parts II, III, and IV). This Court has consistently held, moreover, that selective rate reductions to meet competition may be permissible under the Act. *E.g.*, *Texas & Pac. R. Co.* v. *Interstate Commerce Commission*, 162 U.S. 197; *Interstate Commerce Commission* v. *Alabama Midland Ry.*, 168 U.S. 144, 164; *Interstate Commerce Commission* v. *Chicago G.W. Ry.*, 209 U.S. 108. As a recent congressional staff study observed, "freedom to make spot rates of this type is historic" (*National Transportation Policy*, Preliminary Draft of a Report Prepared for the Senate Interstate and Foreign Commerce Com-

I

A CARRIER'S RATES MAY NOT BE HELD UP TO A PARTICULAR LEVEL MERELY BECAUSE THEY THREATEN THE TRAFFIC, REVENUES OR EVEN THE CONTINUED EXISTENCE OF A COMPETING MODE OF TRANSPORTATION. TO WARRANT A PROHIBITION OF RATE REDUCTIONS ON ECONOMIC GROUNDS, IT MUST BE ESTABLISHED THAT THE COMPETING MODE HAS INHERENT ADVANTAGES WHICH WOULD BE IMPAIRED OR DESTROYED

A. The Legislative History of Section 15a(3) Shows That the Commission May Impose Rate Differentials between Competing Modes of Transportation only when This is a Necessary Means of Preserving the Inherent Advantages of the Respective Carriers

1. The power to prescribe minimum railroad rates was conferred upon the Commission by the Transportation Act of 1920, 41 Stat. 456, 484, amending Section 15(1) of the Interstate Commerce Act, 49 U.S.C. 15(1). Whereas Congress had previously directed its efforts to the prevention of abuses, particularly those stemming from excessive or discriminatory rates, its purpose in the 1920 legislation was to foster a more adequate transportation service and, in particular, to give the Commission power to ensure that carriers received a fair return on their capital. *The New England Divisions Case*, 261 U.S. 184, 190. With the advent of motor carrier regulation in 1935 and water

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mittee by the Special Study Group on Transportation Policies in the United States, 87th Cong., 1st Sess., p. 429). Regardless of the wisdom of terminating this freedom (see a recent bill to that end, S. 3578, 86th Cong., 2d Sess.), we do not believe it can be impaired under present law except under the principles suggested in this brief.

carrier regulation in 1940, the minimum rate power took on added significance.[9] It became one of the primary tools with which the Commission sought to implement the National Transportation Policy declared by Congress in the Transportation Act of 1940, 54 Stat. 899, which, in the words of this Court:

> * * * while intended to secure the lowest rates consistent with adequate and efficient service and to preserve within the limits of the policy the inherent advantages of each mode of transportation, at the same time was designed to eliminate destructive competition not only within each form but also between or among the different forms of carriage.

Eastern-Central Motor Carriers Ass'n v. United States, 321 U.S. 194, 206.[10]

Side by side with the National Transportation Policy, however, Congress developed another set of principles to guide the Commission in fixing rates. In the Emergency Railroad Transportation Act of 1933, 48 Stat. 211, 220, it amended the statement of general regulatory objectives contained in Section 15a(2)

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[9] The minimum rate provisions in Part II of the Commerce Act (motor carriers), Part III (water carriers), and Part IV (freight forwarders) are found in Sections 216(e), 307(b), and 406(b) of the Act.

[10] The importance of the minimum rate power in carrying out these objectives was stressed by the Commission in 1939, when it told the Senate Commerce Committee that "[t]hose who urge equal or impartial regulation of all important forms of transportation lay particular stress upon the need for curbing destructive competition by the fixing of minimum reasonable rates" (Hearings on the Omnibus Transportation Bill before the House Interstate and Foreign Commerce Committee, 76th Cong., 1st Sess., p. 1560).

(which had been added by the 1920 Act, 41 Stat. 488) to direct the Commission to consider "the effect of rates on the movement of traffic."[11] The Transportation Act of 1940, 54 Stat. 899, 912, expanded upon this provision by requiring the Commission to take into account "the effect of rates on the movement of traffic by the carrier or carriers for which the rates are prescribed" (Appendix, *infra*, p. 53). The import of this change was to make clear that "no carrier should be required to maintain rates which would be unreasonable, judged by other standards, for the purpose of protecting the traffic of a competitor" (*Seatrain Lines, Inc.* v. *Akron, C. & Y. Ry. Co.*, 243 I.C.C. 199, 214, 215). It was in response to criticism, chiefly by the railroads, that the Commission had not adhered consistently to the rule of Section 15a(2), but had sought instead to shield carriers from competition[11a] (see *infra*, p. 31), that Congress in 1958 added Section 15a(3).

2. The initial impetus for the legislation which resulted in Section 15a(3) came from a 1955 report entitled *Revision of Federal Transportation Policy*, issued by the President's Advisory Committee on Transport Policy and Organization, under the chairmanship of the Secretary of Commerce. Finding that regulatory policy was urgently in need of revision if the transportation industry was to maintain itself at

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[11] Comparable provisions apply to motor carriers (49 U.S.C. 316(i)), water carriers (49 U.S.C. 907(f)) and freight forwarders (49 U.S.C. 1006(d)).

[11a] For a discussion of the cases in which the Commission was said to have deviated from the rule of Section 15a(2), see Hearings on S. 3778 before the Senate Interstate and Foreign Commerce Committee, 85th Cong., 2d Sess., pp. 86-91.

maximum effectiveness, the report recommended increased reliance on competitive forces in rate-making, maintenance of a modernized and financially strong common carrier system, more efficient and economical management so as to provide the consumer the lowest possible transportation costs, and development of an effective transportation system for defense mobilization or war. Legislation designed to implement these objectives was drafted by the Secretary of Commerce, H.R. 6141, 84th Cong., 2d Sess. It would have revised the National Transportation Policy by eliminating the prohibition against "unfair or destructive competitive practices," and would have amended Section 15a(1) to provide that:

> Sec. 15a. (1) In determining whether a rate, fare, or charge, or classification, regulation, or practice to be applied in connection therewith, results in a charge which is less than a reasonable minimum charge, as used in this Act, the Commission shall not consider the effect of such charge on the traffic of any other mode of transportation; or the relation of such charge to the charge of any other mode of transportation; or whether such charge is lower than necessary to meet the competition of any other mode of transportation: *Provided, however,* That the provisions of this paragraph shall not be construed to prohibit any carrier subject to this Act from protesting or complaining in the event that a rate, fare, or charge is filed or made effective which it believes to be less than a reasonable minimum charge.

This proposal, known as "the three shall-nots," was vigorously supported by the railroads, which argued

that the Commission, in mistaken reliance on the prohibition against "unfair or destructive competitive practices," had undertaken to apportion traffic among the several forms of transportation according to "fair shares" and had rejected even compensatory rail rates on the ground that they would divert from other carriers their allotted share of the traffic. Adoption of the three shall-nots was urged (either as an amendment to Section 15a(1) or in the form of a new Section 15a(3)) in order to restrict the scope of the Commission's inquiry to the question whether a competitive rate was reasonable *per se* and nondiscriminatory, thus in effect limiting the concept of "unfair or destructive competitive practices" to noncompensatory rates. Hearings on H.R. 6141 before the Subcommittee on Transportation and Communications of the House Interstate and Foreign Commerce Committee, 84th Cong., 2d Sess., pp. 532, 537, 540, 548.

The Commission opposed the bill as "inimical to the maintenance of a sound transportation system." It pointed out that since the railroads viewed as compensatory any rate which exceeded out-of-pocket costs, even if it did not cover fully distributed costs, a rate might be "compensatory," yet at the same time enable the railroads to drive out of business a competing carrier with lower full costs, to the ultimate detriment of the public at large which would then be subjected to higher rates. *Id.* at 1768.

Although H.R. 6141 died in committee upon the adjournment of the 84th Congress, the railroads' alternative proposal for a new Section 15a(3) incorporating the three shall-nots was again introduced in

the 85th Congress as H.R. 5523. As before, the railroads made plain that the "underlying purpose" of their bill was to allow them to make competitive rates "without regard to their effect (if any) upon competing modes of transportation." Hearings on Surface Transportation (Ratemaking Legislation) before a subcommittee of the House Interstate and Foreign Commerce Committee, 85th Cong., 1st Sess., pp. 5, 199. The Commission renewed its opposition (*id.* at 46, et *seq.*).

The railroads' proposal was explicitly rejected by a subcommittee of the Senate Commerce Committee, headed by Senator Smathers, which, after extended hearings in the early part of 1958, recommended instead the enactment of a new Section 15a(3) to provide:

> In a proceeding involving competition with another mode of transportation, the Commission, in determining whether a rail rate is lower than a reasonable minimum rate, shall consider the facts and circumstances attending the movement of the traffic by railroad and not by such other mode.

Although the final phrase of the bill was reminiscent of the three shall-nots, it was clearly not intended to restrict the Commission's minimum rate power to the same degree as the measure advocated by the railroads, for the subcommittee expressly stated it was "not convinced that the record before it justifies approval of the railroads' proposal." Report on Problems of the Railroads of the Subcommittee on Surface Transportation of the Senate Interstate and Foreign Commerce Committee, in S. Rep. 1647, 85th Cong.,

2d Sess., pp. 7, 8, 10, 18 (hereafter referred to as "Subcommittee Report").

The full Senate Commerce Committee, which drafted the final version of Section 15a(3) (Appendix, *infra*, pp. 53–54), similarly made plain in its report that the extreme position of the railroads was not to be enacted into law. S. Rep. 1647, *supra*, at 2. The committee version, moreover, was framed largely in response to the warning of the Commission that the concluding phrase of the subcommittee's proposal—"and not by such other mode" was inconsistent with rejection of the three shall-nots. Hearings on S. 3778 Before the Senate Interstate and Foreign Commerce Committee, 85th Cong., 2d Sess., p. 166 (hereafter referred to as "Hearings"); see *infra*, pp. 32–33. The Commission left no room for doubt that its administration of the committee version, if adopted, would include examination of the effect of a rate reduction on competing modes. *Id.* at 178, 181, 183.

Significantly, Congress also rejected proposals, advanced by the Secretary of Commerce, which would have confined the Commission to a consideration of antitrust factors, rather than transportation policy, in reviewing competitive rate-making. Although the Secretary had originally sponsored the three shall-not proposal in the 84th Congress, he opposed its counterpart, H.R. 5523, in the next Congress on the ground that it would exempt the railroads from the responsibilities imposed upon the rest of industry by the antitrust laws, which require consideration of the effect of unreasonably low rates upon competition. In hearings before the subcommitte, the Secretary

suggested language parallel to the Clayton and Robinson-Patman Acts (15 U.S.C. 13–18), under which the Commission might take into account the impact of a rate on competition "only where its effect might be substantially to lessen competition or tend to create a monopoly in the transportation industry or where the rate was established for the purpose of eliminating or injuring a competitor." Hearings on Problems of the Railroads before the Subcommittee on Surface Transportation of the Senate Interstate and Foreign Commerce Committee, 85th Cong., 2d Sess., p. 2353. Later, before the full Commerce Committee, the Secretary again urged the encouragement of competition to the extent possible. He proposed a new Section 15a(3), cast in Sherman Act language, which would allow the Commission, in determining whether proposed rail rates are too low, to consider only whether such rates will "unreasonably restrain trade or commerce" or are part of a monopolization or attempt to monopolize. Such a condition, it was stated, "would prohibit price reductions only when they constituted predatory practices which threatened the existence of the competitive system itself." Hearings, supra, at 198, 199. The Secretary's proposals received virtually no mention during the pendency of Section 15a(3) before Congress.[11]

[11] The only explicit reference is in the individual views of Senator Lausche, appended to the subcommittee report. While concurring in the proposed addition to Section 15a, he "recognize[d] that strong arguments can be made that the subcommittee should have gone further and followed the [Clayton Act] suggestions made by the Secretary of Commerce on the subject" (Subcommittee Report, *supra*, at 28). The majority

It is clear, therefore, that Section 15a(3) was not intended to preclude the Commission from considering, in terms of national transportation policy, the effect of reduced rates on competing modes of carriage.

3. Nevertheless, the most significant feature of Section 15a(3) is its prohibition against holding up the rates of one mode to protect another, expressing the congressional intent to encourage competition in the public interest. The legislative history indicates further that the primary purpose of the qualifying provision—referring to the National Transportation Policy—was to meet the objection that otherwise the Commission would be disabled from dealing with rates which were predatory, or destructive in the sense that they would undermine the inherent advantages of competing media rather than assert legitimately the advantages of the rate proponent.

The railroads had urged, in support of the three shall-nots, that their inherent advantage of low cost should be made available to the shipping public. While rejecting the railroads' proposal in favor of its own draft (*supra*, p. 27), the subcommittee proclaimed as its policy, and the policy of Congress, "that each form of transportation should have opportunity to make rates reflecting the different inherent advantages each has to offer so that in every case the public may exercise its choice, cost and service both con-

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characterized this as a belief "that the amendment recommended does not give sufficient freedom for making competitive rates" (*id.* at 18–19). Senator Lausche later concurred in the Committee recommendation.

sidered, in the light of the particular transportation task to be performed." It added, however, that "such rate-making should be regulated by the Commission to prevent unfair destructive practices on the part of any carrier or group of carriers." Pointing out that the Commission had not consistently adhered to the "inherent advantage" principle, the subcommittee report stated that the purpose of amending Section 15a was to "admonish the Commission to be consistent in following the policy" it had enunciated in *New Automobiles in Interstate Commerce*, 259 I.C.C. 475, 538, where it found no warrant for believing that the rates of one mode should be held up to preserve another.[12] Finally, the subcommittee quoted with approval the following language of this Court in *Schaffer Transportation Co.* v. *United States*, 355 U.S. 83:

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[12] In *New Automobiles*, the Commission had approved reduced rail rates protested by motor carriers for the carriage of automobiles. In its report, the Senate subcommittee quoted the Commission statement (259 I.C.C. at 538) that in enacting "separately stated rate-making rules for each transport agency, [Congress] obviously intended that the rates of each such agency should be determined by [the Commission] in each case according to the facts and circumstances attending the movement of the traffic by that agency. In other words, there appears no warrant for believing that rail rates, for example, should be held up to a particular level to preserve a motor-rate structure * * *." The subcommittee declared its intention "to affirm the interpretation of the Commission given in the *Automobile* case epitomized in the words quoted above," which had "properly construed the intent of Congress" that "the Commission consistently follow the principle of allowing each mode of transportation to assert its inherent advantages, whether they be of service or of cost" (Subcommittee Report, *supra*, at p. 3).

> To reject a motor carrier's application on the bare conclusion that existing rail service can move the available traffic, without regard to the inherent advantages of the proposed service, would give one mode of transportation unwarranted protection from competition from others.
>
> * * * * *
>
> The ability of one mode of transportation to operate with a rate lower than competing types of transportation is precisely the sort of "inherent advantage" that the congressional policy requires the Commission to recognize.

S. Rep. No. 1647, *supra*, at 18–19.

The subcommittee amendment was the subject of extended testimony in hearings conducted by the full Senate Commerce Committee in May 1958. Chairman Freas, testifying on behalf of the Commission, expressed full agreement with the principles set forth in the subcommittee report, stressed the wisdom of protecting the inherent advantages of each mode (Hearings, *supra,* at 167, 171), and noted that except for its concluding phrase—"and not by such other mode"—the subcommittee proposal was substantially equivalent to Section 15a(2) as it then stood (*id.* at 166–167). The Chairman cautioned, however, that the quoted phrase was inconsistent with the subcommittee's stated objective of preventing unfair destructive practices, since these could not be ascertained without examining the effect of a rate on competing forms of transportation (*id.* at 167–168). Along the same lines, he observed that while a purpose of rate regulation should be to encourage the flow of traffic by the most economical means, this means could not

be identified without considering the circumstances attending the movement of traffic by transportation modes other than the one proposing the rate (*id.* at 168). The uncertain purpose of the amendment, he warned, would enable the railroads to argue that they were intended to have complete freedom, in the face of competition from another mode, to establish rates which merely covered out-of-pocket costs (*id.* at 167).

Chairman Freas then urged that the "real questions" presented by the amendment, on which Congress should make its intention unmistakably clear, were the following:

> (1) "*whether Congress desires to give to the high-cost carrier in every competitive-rate situation complete discretion to establish any rates which cover its out-of-pocket costs without regard to its effect upon the ability of the low cost carriers to move the particular traffic at rates which cover all of their cost,*" and (2) whether and to what extent Congress desires to prohibit the maintenance of minimum rates on high value commodities at a level higher than would be justified by cost considerations alone. [Emphasis added.]

The crux of the first problem, as the Chairman saw it, was that while transportation should, circumstances permitting, return the full cost of performing the service, in many instances the full cost of the low-cost mode exceeds the out-of-pocket cost of another. "If, then," he said "we are required to accept the rates of the high cost carrier merely because they exceed its out-of-pocket costs, we see no way of preserving the inherent advantages of the low

cost carrier. In any event, that other mode would be compelled to depress its rates below full costs in order to preserve its inherent advantages against the high cost form of transportation" (*id.* at 168).

The same point—*i.e.*, that a rate might be "compensatory" in the sense of covering out-of-pocket costs and yet infringe upon the inherent advantage of a more economical carrier—was reemphasized later in the Chairman's testimony when he explained that the lawfulness of a challenged rate deduction (*id.* at 172)—

> depends in each instance on which form of transportation is the low-cost form * * *
>
> Now, if it is a case where the railroad is a low-cost form of transportation, again, there is no objection to be made to that. But if the railroad is the high-cost form of transportation, I do not think that the fact that the railroad would get 50 cents a ton or 2½ cents a hundred pounds [above out-of-pocket costs] out of that traffic would override the interest of the general public in being able to have that same traffic hauled by the low-cost form of transportation at possibly a lower rate and at a full profit to the other form of transportation merely—rather than just 2½ cents above the out-of-pocket cost.[13]

Presumably to remedy the ambiguity of the subcommittee's draft as it related to these problems, the

[13] See also colloquy between Senators Smathers and Kefauver, 104 Cong. Rec. 10858–10859, in which Senator Smathers apparently agreed that the amendment would prohibit a rate which, by failing to return full costs, would infringe the inherent advantage of a competing lower-cost mode.

Chairman proposed (*id.* at 169) the following substitute:

> In a proceeding involving competition between carriers, the Commission, in determining whether a proposed rate is lower than a reasonable minimum rate, shall consider the facts and circumstances attending the movement of the traffic. Rates of a carrier shall not be held up to a particular level to protect the traffic of a less economic carrier, giving due consideration to the inherent cost and service advantages of the respective carriers.

Senator Smathers suggested that the Commission's objections could be met by adding to the subcommittee's language "that the Commission will always, should always have the right to consider whether an application for a rate falls within * * * the purview of unfair destructive rate practice" (*id.* at 170). He also intimated that the controversial concluding phrase of the subcommittee proposal ("and not by such other mode") might well be overridden by the national transportation policy even without any express qualification (*id.* at 177). When the Chairman expressed doubt on these questions, Senator Smathers proposed the addition to the subcommittee proposal of a direction that the Commission "always [keep] * * * in mind the provision of the national transportation policy which the Congress approved in 1940 and reaffirms here now" (*ibid.*). Senator Potter, who was a member of the full Committee, but not of the subcommittee, suggested the adoption of Senator Smathers' new phrase and the deletion of the phrase "and not by such other mode," and Chairman Freas indicated that this revision would be acceptable (*ibid.*).

Other witnesses also objected to the subcommittee bill, chiefly on the ground that it will allow the railroads, by reducing their rates below a fully compensatory level, to overcome the inherent cost advantages of competing modes. For example, John L. Weller, testifying on behalf of Seatrain Lines and Pan-Atlantic Steamship Corp. (now Sea-Land) replied as follows to a question by Senator Potter:

> Senator POTTER. * * * You want to have the inherent advantages of water transportation protected, so that unfair competition can't move you out of your traffic; is that right?
>
> Mr. WELLER. That is right, Senator. I want no more than what is fair.
>
> As I explained, our kind of operation can only exist with a differential under the railroad rates; that is No. 1. We are not entitled to have such a differential, nor do I urge one, except in the case where cost is lower than the railroad cost. We have no right to ask for anything more than that. But if we are to be exposed to rate-cutting practices by the railroads, for instance, in which the railroads are going to cut their rates on an out-of-pocket cost basis and to subject me at the same time to local rates which put me in a squeeze, obviously we cannot continue in business. * * * [*id.*, at 30].

See also testimony of A. C. Ingersoll, Jr., representing the barge lines (*id.* at 107).

Despite the distinctions between the subcommittee proposal and that of the full Commerce Committee, the committee report made plain that there was no fundamental change in objective. The committee re-

produced and expressly approved almost the entire discussion of competitive ratemaking in the subcommittee report (S. Rep. 1647, *supra*, at 2). It then described its new proposal as "designed to encourage competition * * * by allowing each form of transportation * * * full opportunity to make rates reflecting the inherent advantages each has to offer * * *" (*id.* at 3), and stated that such ratemaking would be "regulated by the Interstate Commerce Commission * * * to prevent 'unfair or destructive competitive practices' as contemplated by the declaration of national transportation policy" (*id.* at 3; see the parallel statement of the subcommittee, *supra*, p. 30). According to the committee, the effect of its proposal would be to put "the principal emphasis, but not the exclusive emphasis, in a competitive ratemaking proceeding involving different modes of transportation * * * on the conditions surrounding the movement of the traffic by the mode to which the rate applies" (*id.* at 3–4).

The House view of Section 15a(3) paralleled that of the Senate. The House Commerce Committee report on H.R. 12832, which embodied the Senate Committee version, restated almost verbatim the approval accorded by both Senate reports to *New Automobiles* and *Schaffer Transportation Co.* v. *United States* (H. Rep. 1922, 85th Cong., 2d Sess., pp. 13–14); exhorted the Commission to "follow the principle of allowing each mode of transportation to assert its inherent advantages"; and declared that "the effect of this amendment will be to encourage competition between the different modes of transportation for the benefit of

the shipping public," thereby providing "a guide to the Commission in achieving consistency in its treatment of competitive rate cases" and ending the agency's vacillation between the *New Automobiles* philosophy and paternalism (*id.* at 14–15).

The purpose of Congress to protect the inherent advantages of all competing modes of transportation was repeatedly manifested in the debates on Section 15a(3). Senators Schoeppel (104 Cong. Rec. 10817), Lausche (*id.* at 10822, 10842, 10859), and Potter (*id.* at 10842), all members of the subcommittee which had considered earlier versions, made plain that this was their intent, as did Senator Bricker (*id.* at 10842). Similar views were expressed by Representative Harris (*id.* at 12531) and various members of his House Commerce Committee (*id.* at 12524, 12531–12532, 12536).

The foregoing account makes clear, we think, that it was not the intent of Congress to give the Commission with one hand what it had taken away with the other—namely, the power to act as a "giant handicapper," [14] establishing whatever differentials might be necessary to equalize the race, or at least assure that no runner would drop out. Instead, its purpose was a limited one: to make certain that price reductions to less than fully compensatory levels—which, in the hearings and debates were referred to as "destructive competitive practices" [15]—would not obliterate the natural cost advantage enjoyed by a competing form of

[14] See Hearings, *supra*, at 82.

[15] See *id.* at 170, 176–177; 104 Cong. Rec. 10859, 12531–12532.

carriage. It follows, we think, that in the absence of a finding that the water carriers were the low-cost mode on the movements to which the proposed TOFC rates applied, the Commission was without authority to cancel those rates, whether or not they exceeded fully distributed costs. Moreover, as we now show, even if the Commission be deemed to have made a finding that Sea-Land was the low-cost mode on this traffic, it was still not empowered to cancel the TOFC rates which were fully compensatory, at least in the absence of a finding (not in fact made), that the water carrier required rates in excess of fully distributed costs on these movements to compensate for deficits incurred in moving other traffic.

B. The Finding that a Competing Mode of Transportation Is the Low-Cost Medium on Particular Traffic Is Not of Itself Sufficient to Warrant the Cancellation of a Fully Compensatory (Though Reduced) Rate Proposed by the High-Cost Mode.

Although the Commission declared itself unable to determine where the inherent advantages lay as to the rates in controversy, and held that considerations other than relative costs were dispositive of the issues before it, it stated, nonetheless, that the Sea-Land costs, both out-of-pocket and fully distributed, were less than the corresponding costs of the railroads' TOFC service on all but two movements. (R. 36–37). The question arises, then, whether this finding—assuming it be such—was enough to justify the Commission's action in holding an umbrella over the Sea-Land rates.

We note preliminarily that, although the district court set aside the entire "order requiring cancellation of the TOFC rates," it enjoined the Commission from cancelling on remand only those rates "which return at least the fully-distributed cost of carriage." (R. 258, 262). Presumably, therefore, it remains open to the Commission, even without additional findings, to disallow the TOFC rates—applicable to 23 of the 66 movements by railroad-leased TTX cars and to 43 of the 66 movements by railroad-owned cars (R. 22)—which equalled or exceeded out-of-pocket costs but fell short of fully distributed costs. If the railroads were dissatisfied with the terms of the court's mandate, it was incumbent upon them to challenge those terms by a timely appeal to this Court. Since they have failed to do so, we assume that they are now precluded from raising any objection to the cancellation of the less than "fully compensatory" rates and that the disposition of those rates is not an issue before this Court. Accordingly, we shall confine our argument to those rates which would return the railroads their fully distributed costs.

The district court, we have concluded, was correct in holding that the cancellation of these rates was improper. In order to justify the disallowance of a proposed rate reduction because of its impact on a competitor, it is not enough to find that the competitor possesses an inherent cost advantage. It must also be found that the proposed rate will destroy, or at least impair, that cost advantage. Such impairment occurs, we submit, when the low-cost carrier is unable to fix a rate which (a) covers its fully distributed

costs and (b) affords it in a rate advantage (as against the high-cost carrier) which is no less than the cost differential (measured in terms of fully distributed costs) between the two modes.

Certainly, then, in ordinary circumstances, a rate which exceeds the fully distributed costs of the high-cost carrier cannot be deemed "destructive." Conceivably in some instances the low-cost mode may require for particular movements a rate significantly higher than fully distributed costs in order to offset revenue deficiencies on other freight which will not move at a fully compensatory rate; in such cases, there might be justification for maintaining a differential at levels higher than would otherwise be warranted. But the Commission made no finding here that there was a need to subsidize the movement of other traffic.[16] Moreover, we do not believe that its

[16] The district court's opinion does not conflict with this conclusion, although it suggests certain qualifications upon the Commission's power to engage in "value-of-service" rate-making. See note 5, p. 11, *supra*. Since, in any event, the Commission has not purported, in this case, to fix the level of the rates on the basis of a need to subsidize other forms of traffic, this issue is not presented in concrete form, and we doubt that the Court should attempt to determine abstractly the various factors which the Commission might take into account and the lengths to which it might go. The Commission has recently described the type of record which it believes adequate to sustain a decision on value-of-service grounds (*Motor Vehicles—Kansas City to Arkansas, Louisiana & Texas*, I. & S. Dkt. No. 7269, decided September 21, 1962, p. 31):

"On the other hand, there is no sufficient or specific evidence to substantiate the claim of the complainant-protestant that the rail rate structure as a whole requires that the involved automobile traffic return considerably more than fully distributed

action in cancelling these TOFC rates can be supported on the ground of forestalling an anticipated series of retaliatory rate reductions which might leave unaltered the original differential between the two modes but drive the rates down to less remunerative levels. So long as the rates remain fully compensatory, the Commission is required to stay its hand, in keeping with the express policy of the Act to provide the public "adequate and efficient railway transportation service at the lowest cost consistent with the furnishing of such service." See 49 U.S.C. 15a(2).

That the Commission should not ordinarily be permitted to disallow a fully compensatory rate was brought out in the House debates on the present form of Section 15a(3). Representative Allen (a member of the House Commerce Committee, which reported the bill) attributed to the bill a purpose "to promote healthy rate competition between the different forms of carriage" by giving each mode "greater free play in establishing reduced rates if those rates are compensatory and do not discriminate unjustly among shippers," in order to "enable the public to enjoy the obvious benefits of relatively lower rates where any mode of transportation can offer such rates and still show a profit" (104 Cong. Rec. 12524). Representative Harris, Chairman of the House Committee, emphasized (*id.* at 12531) that:

> if a carrier can provide a rate that is fully compensatory to the shipping public the Commis-

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costs in order that the so-called low-grade deficit freight and less-carload and passenger service be subsidized, or what the particular extent of such contribution should be."

> sion cannot * * * require that carrier to hold that rate up to a higher level just because it is necessary to keep another mode of transportation in business * * * [I]f a carrier can provide a rate which the Commission determines is fully compensatory to the carrier, then the shipper should have the benefit of that rate.

In the same vein, Representative O'Hara stated that the language plainly meant that if the rate is "compensatory" to the proponent, the Commission "would have to allow that competing form of transportation to charge a lower rate" (*id.* at 12536); and Representative Avery, referring to the Commission decision in *New Automobiles*, stated that while the Commission "is not required" to hold up rates merely to protect a competing mode, "[i]t is required however to only approve a rate that is fully compensatory to the common carrier for that service" (*id* at 12538).

There is no guarantee, to be sure, that Sea-Land would be able to attract business at a differential which no more than reflected its inherent cost advantage. The Commission estimated that in order to be competitive the water carriers might require a margin approximately 6 percent below the TOFC rate for given movements (R. 41–42), and it made no finding as to whether the cost differences between the two forms of carriage were greater or less than this margin. It is conceivable that the superiority of the railroads' service—its greater speed, frequency, and dependability—would be valued more highly by a majority of shippers than the cost savings offered by

that the overriding needs of national defense (and perhaps commerce as well) might, upon an appropriate showing, warrant the exercise of the minimum rate power to preserve a threatened carrier.

We have shown *supra*, p. 30–37, that the primary purpose of Congress in qualifying the basic prohibition contained in Section 15a(3) was to make clear that the Commission would be free to prevent "destructive competitive practices" which threatened to infringe the inherent advantages of a competing mode. It is significant, however, that Congress chose not to accept the language proposed by the Commission, which would have expressed the qualification in terms of the inherent-advantage factor alone, *supra*, p. 34, but, instead, adopted the broader reference to the National Transportation Policy as a whole. We see no justification for the district court's view that the general and ultimate objectives proclaimed in the concluding clause of the Policy should be dismissed as verbal paraphernalia while only the specific policy factors previously enunciated are taken seriously. Moreover, in 1958 the National Transportation Policy had long been construed as authorizing the Commission to act on the basis of national defense requirements. *United States* v. *Capital Transit Co.*, 338 U.S. 286, 290; *United States* v. *Capital Transit Co.*, 325 U.S. 357, 361–362; *Cantlay & Tanzola, Inc.* v. *United States*, 115 F. Supp. 72, 80–81 (S.D. Cal.). The Commission had, indeed, developed a limited but well-established practice of relying upon the national defense clause to act in appropriate cases when no other authority was available. See, *e.g.*, *Increased*

Common Carrier Truck Rates in the East, 42 M.C.C. 633, 650; *Novick Extension of Operations—Explosives*, 34 M.C.C. 693, 697; *Kiser and Countryman Extension of Operations*, 31 M.C.C. 127, 131. Moreover, the existence of the national defense element in the National Transportation Policy was explicitly recognized by Representative Harris during his statement on the House floor in connection with the section of the 1958 Act which followed Section 15a(3), dealing with exemption of transportation of agricultural commodities from regulation. 104 Cong. Rec. 12531–12532.

This is not, of course, to say that the broad conclusory language of the National Transportation Policy relating to national needs is to be freely applied so as to render inoperative the specific policy factors which precede it or the basic *laissez faire* philosophy expressed in Section 15a(3). If that Section means anything at all, it means that in the ordinary case of intermodal competition, the Commission should not interfere with a rate which is fully compensatory and which therefore either asserts the inherent cost advantage (if any) of the proponent or at least does not infringe upon the inherent cost advantage (if any) of the competitor. Occasionally, however, a carrier which lacks any widely demanded economic advantage and which cannot attract enough business to operate at a profit may yet be uniquely equipped to perform a service vital to the military establishment or a significant segment of commerce. An obvious example would be a carrier which could transport missiles more safely and expeditiously than

any other mode. Moreover, there may be instances in which the facilities of the uneconomical mode are of great potential importance in the event of a national emergency. This might well be true of the water carriers in the present case. In such circumstances, we submit, the prohibition against umbrella ratemaking might properly give way to the requirements of the national defense (or commerce).

The showing, however, must be more than perfunctory. It must be demonstrated, first, that the proposed rate genuinely threatens to destroy a competing mode of transportation and, secondly, that the threatened mode is able to fill a vital national defense or other public need which could not be adequately filled by any other available form of carriage. We suggest that evidence of national defense requirements might take the form of expert testimony by representatives of the government agencies operating in that area, such as the Department of Defense or the Office of Emergency Transportation in the Department of Commerce. In any event, however, the evidence must relate to the specific carrier which seeks protection and should set forth with particularity the reasons why the survival of this carrier is important to the national defense. A similar standard should apply where the Commission relies on the commerce factor. It then becomes the task of the Commission to decide whether the considerations favoring protective action outweigh the basic principles of competitive ratemaking contemplated by Section 15a(3) and the National Transportation Policy.

The findings and evidence here do not meet this test. Although the Commission concluded that the reduced TOFC rates were "an initial step in an overall program of rate reductions that can fairly be said to threaten the continued operation, and thus the continuing existence of the coastwise water-carrier industry generally" (R. 38), it made no specific findings to support this conclusion. In particular, it did not find whether reductions in the water carriers' rates to restore the differential which existed prior to the TOFC reductions would render the water carrier rates unprofitable. Moreover, there were neither findings nor substantial evidence as to the manner in which the national defense requires Sea-Land's survival. As indicated above, the Commission relied entirely on studies prepared by two government bodies, one of which, made in 1955, stressed the national defense role of break-bulk vessels such as Sea-Land no longer operates (*supra*, p. 4); while the other, dated 1950, merely referred in passing to the role of coastwise shipping in providing tonnage for emergency use. The Commission's suggestion of the commerce factor was similarly diffuse. We agree, therefore, with the district court that the report of the Commission fails to supply the evidence and findings required to sustain a decision on national defense (or commerce) grounds. At the same time, we urge that the district court's interpretation of this aspect of the National Transportation Policy is unduly restrictive and that the Commission, upon a remand of the case, should have greater latitude than the opinion below would permit.

CONCLUSION

The judgment of the district court should be vacated and the cause remanded to the Commission for further proceedings in conformity with the principles herein set forth.

Respectfully submitted.

ARCHIBALD COX,
Solicitor General.
LEE LOEVINGER,
Assistant Attorney General.
FRANK I. GOODMAN,
Assistant to the Solicitor General.
LIONEL KESTENBAUM,
JOEL E. HOFFMAN,
Attorneys.

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APPENDIX

STATUTES INVOLVED

The National Transportation Policy, 49 U.S.C. preceding Sections 1, 301, 901, and 1001, provides:

> It is hereby declared to be the national transportation policy of the Congress to provide for fair and impartial regulation of all modes of transportation subject to the provisions of this Act, so administered as to recognize and preserve the inherent advantages of each; to promote safe, adequate, economical, and efficient service and foster sound economic conditions in transportation and among the several carriers; to encourage the establishment and maintenance of reasonable charges for transportation services, without unjust discriminations, undue preferences or advantages, or unfair or destructive competitive practices; to cooperate with the several States and the duly authorized officials thereof; and to encourage fair wages and equitable working conditions;—all to the end of developing, coordinating, and preserving a national transportation system by water, highway, and rail, as well as other means, adequate to meet the needs of the commerce of the United States, of the Postal Service, and of the national defense. All of the provisions of this Act shall be administered and enforced with a view to carrying out the above declaration of policy.

Section 15(7), 49 U.S.C. 15(7), provides:

> Whenever there shall be filed with the Commission any schedule stating a new individual or joint rate, fare, or charge, or any new indi-

vidual or joint classification, or any new individual or joint regulation or practice affecting any rate, fare, or charge, the Commission shall have, and it is hereby given, authority, either upon complaint, or upon its own initiative without complaint, at once, and if it so orders without answer or other formal pleading by the interested carrier or carriers, but upon reasonable notice, to enter upon a hearing concerning the lawfulness of such rate, fare, charge, classification, regulation, or practice; and pending such hearing and the decision thereon the Commission, upon filing with such schedule and delivering to the carrier or carriers affected thereby a statement in writing of its reasons for such suspension, may from time to time suspend the operation of such schedule and defer the use of such rate, fare, charge, classification, regulation, or practice, but not for a longer period than seven months beyond the time when it would otherwise go into effect; and after full hearing, whether completed before or after the rate, fare, charge, classification, regulation, or practice goes into effect, the Commission may make such order with reference thereto as would be proper in a proceeding initiated after it had become effective. If the proceeding has not been concluded and an order made within the period of suspension, the proposed change of rate, fare, charge, classification, regulation, or practice shall go into effect at the end of such period; but in case of a proposed increased rate or charge for or in respect to the transportation of property, the Commission may by order require the interested carrier or carriers to keep accurate account in detail of all amounts received by reason of such increase, specifying by whom and in whose behalf such amounts are

paid, and upon completion of the hearing and decision may by further order require the interested carrier or carriers to refund, with interest, to the persons in whose behalf such amounts were paid, such portion of such increased rates or charges as by its decision shall be found not justified. At any hearing involving a change in a rate, fare, charge, or classification, or in a rule, regulation, or practice, after the date this amendatory provision takes effect, the burden of proof shall be upon the carrier to show that the proposed changed rate, fare, charge, classification, rule, regulation, or practice is just and reasonable, and the Commission shall give to the hearing and decision of such questions preference over all other questions pending before it and decide the same as speedily as possible.

Section 15a, 49 U.S.C. 15a, provides:

(1) When used in this section the term "rates" means rates, fares, and charges, and all classifications, regulations, and practices relating thereto.

(2) In the exercise of its power to prescribe just and reasonable rates the Commission shall give due consideration, among other factors, to the effect of rates on the movement of traffic by the carrier or carriers for which the rates are prescribed; to the need, in the public interest, of adequate and efficient railway transportation service at the lowest cost consistent with the furnishing of such service; and to the need of revenues sufficient to enable the carriers, under honest, economical, and efficient management to provide such service.

(3) In a proceeding involving competition between carriers of different modes of transportation subject to this Act, the Commission,

in determining whether a rate is lower than a reasonable minimum rate, shall consider the facts and circumstances attending the movement of the traffic by the carrier or carriers to which the rate is applicable. Rates of a carrier shall not be held up to a particular level to protect the traffic of any other mode of transportation, giving due consideration to the objectives of the national transportation policy declared in this Act.

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